



GENERAL ASSEMBLY OF THE STATE OF TENNESSEE FISCAL REVIEW COMMITTEE

320 Sixth Avenue, North – 8th Floor
NASHVILLE, TENNESSEE 37243-0057
615-741-2564

Rep. Charles Curtiss, Chairman
Representatives

| | |
|---|---------------|
| Curt Cobb | Donna Rowland |
| Curtis Johnson | David Shepard |
| Gerald McCormick | Curry Todd |
| Mary Pruitt | Eddie Yokley |
| Craig Fitzhugh, <i>ex officio</i> | |
| Speaker Jimmy Naifeh, <i>ex officio</i> | |

Sen. Douglas Henry, Vice-Chairman
Senators

| | |
|--|---------------|
| Bill Ketron | Reginald Tate |
| Doug Jackson | Jamie Woodson |
| Paul Stanley | |
| Randy McNally, <i>ex officio</i> | |
| Lt. Governor Ron Ramsey, <i>ex officio</i> | |

ANNUAL REPORT OF THE CONTRACT SERVICES SUBCOMMITTEE TO THE GENERAL ASSEMBLY

JANUARY 5, 2009

Introduction

This report is submitted to the General Assembly by the Contract Services Subcommittee pursuant to Tenn. Code Ann. § 3-7-112(g) concerning the work of the Subcommittee during calendar year 2008. The Subcommittee undertakes special investigations to identify and improve contracting practices that potentially jeopardize the state's fiscal position. In addition, the Subcommittee has an ongoing statutory responsibility to review each proposed state non-competitive contract and contract amendment with a term of more than one year and a cumulative maximum liability of \$250,000 or more pursuant to Tenn. Code Ann. § 12-4-109(a)(1)(G) to determine whether the contract and its proposed method of procurement are in the State's best interest. This report describes the Subcommittee's activities in 2008 to fulfill both of these responsibilities.

Special Investigations

1. Child placement contracts.

In January, 2008, the Subcommittee authorized the staff to investigate the use of special delegated authorities by the Department of Children's Services (DCS) for

child placement contracts. This investigation was conducted in response to a request from the Senate Government Operations Committee to address concerns about the level of oversight and checks and balances in the expenditures of large sums of state dollars. The staff presented its findings at a hearing of the Senate Government Operations Committee on January 16, 2008. The staff's full presentation is posted on the Fiscal Review Committee's webpage under the Presentations tab.

The investigation found that DCS had entered into 155 contracts for child placement with a cumulative value of \$539 million, of which \$432 million had already been committed, under a "special delegated authority" (SDA) under rules of the Department of Finance and Administration (F&A). SDAs are intended to give departments some latitude in negotiating standardized contracts with providers of services subject to general parameters mutually agreed to by the contracting department, F&A, and the Comptroller of the Treasury as part of the SDA.

The staff did not find any abuse or improper behavior in connection with the DCS contracts. From a process perspective, however, the investigation revealed that these contracts were not subject to the oversight and checks and balances applicable to most state contracts and that there was substantial potential for abuse in the system. There was no review of these contracts by F&A's Office of Contract Review (OCR) or the Comptroller. Contracts could be entered into and expenditures incurred on the sole authority of the commissioner of the contracting department. There were no safeguards outside of the constraints imposed by the contracting department itself to prevent potential abuse of the system, including favoritism in the awarding of contracts or unwarranted payments.

The investigation resulted in enactment by the General Assembly of Public Chapter 933 (2008) requiring any department utilizing an SDA to provide the Fiscal Review Committee a quarterly report of all contracts entered pursuant to the SDA, including the name of the contractor, contract amount, contract term, and completion date for a contract monitoring review. F&A has undertaken a greater oversight role on these contracts as well. These changes will enable the General Assembly to exercise greater oversight over these contracts to ensure that SDAs are not abused. The quarterly reports are maintained in the Fiscal Review Committee offices and are available for review by members of the General Assembly and the public.

2. Accounting for unspent dollars in state contracts.

The Subcommittee has focused attention in its public hearings on non-competitive contracts on the difference between amounts allocated for contracts in a given year and the amount actually spent. In many cases, but not all, the contracting department allocates funds for contracts in excess of actual anticipated expenditures.

This excess allocation is cumulatively reflected in excess maximum liability for contracts.

The excess allocation and overstatement of maximum liability appears to result from a desire by departments to avoid the somewhat cumbersome process of amending contracts to request additional spending authority. It does not appear to affect departmental budgets and appropriations since they are program-driven and are not compiled based on anticipated individual contract spending.

The Subcommittee is conducting an ongoing review of this process with an aim of making contract allocations and maximum liabilities more closely match actual and anticipated expenditures. Thus far the investigation has revealed that a department may spend, subject to budget and appropriations limitations, any amount on a contract in any year provided the maximum liability is not exceeded.

This policy is designed to give departmental fiscal and contracting officers maximum flexibility in managing contracts, but it also makes ongoing monitoring and oversight of those contracts by outside entities, including the Subcommittee, more difficult. The Subcommittee reviews, among other things, whether a proposed expenditure is reasonable for the services to be provided. This evaluation is severely distorted if the department has reported an unrealistically high contract allocation and maximum liability. Given the large amount of state funds expended through contracts, the Subcommittee believes that allocations and maximum liabilities should be more closely matched with actual anticipated expenditures.

The Subcommittee staff is working with F&A to develop a mechanism to meet these concerns without depriving departments of necessary flexibility in managing contracts. These discussions will continue in 2009. Once a resolution of this issue has occurred, the Subcommittee will report the result to the General Assembly.

Ongoing Review of Non-Competitive Contracts

In 2008, the Subcommittee conducted 14 days of public hearings on proposed non-competitive contracts and contract amendments. The Subcommittee reviewed 172 contracts and amendments with a cumulative maximum liability of \$24,868,513,484.

Among other contracts, the Subcommittee reviewed a proposed contract between the University of Tennessee and the University of Tennessee Research Foundation for administrative and other management services pertaining to the University's switchgrass to ethanol biofuels initiative. The Subcommittee expressed concern about the lack of legislative oversight over the expenditure of state funds appropriated to support this initiative. The University has agreed to provide the Subcommittee with

detailed periodic reports on expenditures and progress on the project. The details of this reporting are still being finalized.

Conclusion

Billions of dollars are spent each year through contracts and it is imperative that direct legislative oversight of these practices occur to ensure accountability for the expenditure of these funds. The Subcommittee will continue to pursue vigorous oversight of State contracting practices. Complete files on the Subcommittee's activities are available at the Fiscal Review Committee offices.

Respectfully submitted,

A handwritten signature in cursive script, reading "Bill Ketron". The signature is fluid and stylized, with a long horizontal stroke at the end.

Senator Bill Ketron, Chairman
Contract Services Subcommittee